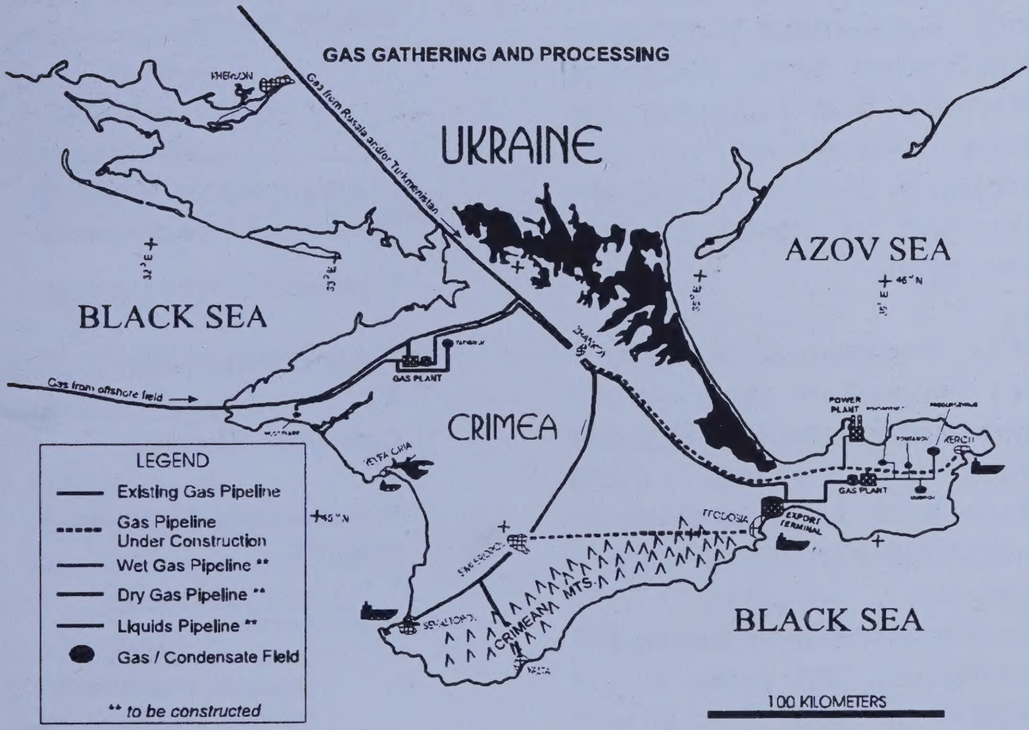
EPIC ENERGY



1996 Annual Report

Epic Energy Inc. is a rapidly growing, international oil and gas exploration, development and production company based in Calgary, Alberta. The Company was established in 1992 as OTM International Development Inc. Subsequent to listing on the Alberta Stock Exchange in 1994 and acquiring the large Ukraine oil and gas project in 1995, the Company changed its name to Epic Energy Inc.

The Company's operations are focused on development and production of oil and gas from numerous field discoveries within its Crimean production sharing acreage.

Having drilled four successful production test wells in the Aktash oil field, Epic is well positioned with new financing to rapidly expand production during the coming year.

Epic is traded on the Alberta Stock Exchange under the symbol: **EPI**.

ANNUAL MEETING

The Annual General Meeting of Shareholders will be held at 10:00 a.m. on Thursday, December 19, 1996, in the Barclay Room of the Westin Hotel, 320 - 4th Avenue S.W., Calgary, Alberta.

TABLE OF CONTENTS

Highlights
1

Letter to Shareholders
2

Operations Review
5

Management's Discussion & Analysis
9

Attachments
- **Auditors' Report**
- **Financial Statements**
- **Notes to the Financial Statements**

Corporate Information (back cover)

NOTE: all financials are in US dollars

HIGHLIGHTS

FINANCIAL

(US$ 000, except per share amounts)	1996	1995
Revenue	19	NIL
Cash Flow from Operations	(2,247)	(1,218)
Per Share	(0.059)	(0.042)
Net Earnings (Loss)	(2,196)	(1,568)
Per Share	(0.058)	(0.054)
Total Oil & Gas Interests	6,676	6,052
Long-term Debt	280	280
Shareholders' Equity	5,759	4,716

OPERATIONS

	1996	1995
Production Capability		
Oil (BBLS/D)	600	-
Average Sales Price		
Oil (US$/BBL)	18.50	-
Reserves — Proven & Probable[1]		
Oil and NGLs (MBBLS)	see footnote	see footnote
Gas (BCF)	see footnote	see footnote
Wells Drilled	3	1
Land Holdings (Acres)	7 million	7 million

---

[1] The Company's Proven & Probable Reserves numbers will be announced when the independent engineering study has been completed and published.

LETTER TO SHAREHOLDERS

We are pleased to present the annual report for Epic Energy Inc. for the year ended June 30, 1996. The Company's focus has been on its Crimea, Ukraine, oil and gas properties. At the field and executive levels, it has been a year of testing: of the Aktash oil reservoirs for optimum production and of our ability to operate economically in the midst of Ukraine's rapidly evolving laws, rules and regulations.

Corporate offices were moved from Vancouver to Calgary and Epic's formal incorporation status was *continued* from British Columbia to Alberta, which means that Epic is now an Alberta corporation.

There were several private placements completed during the year. These were essential to the ongoing operations while the Company strived to complete a large financing that would capitalize the full development of the shallow oil fields plus the comprehensive evaluation of the deeper gas-condensate field discoveries. A total of 3,521,923 special warrants were issued by the Company for a gross proceeds of US$2,180,338. Assuming 100% exercise of issued share purchase warrants, Epic could realize an additional US$2,483,326 in equity investment funds.

Milestones

The Company reached some critical milestones during the reporting year.

- On the Corporate level, Epic's Board of Directors was substantially upgraded when Robert O. Anderson accepted the position of Chairman and John Zaozirny, Laurence Decore and Bobby Long were elected to the Board at the Annual General Meeting in December, 1995.
- Operationally, on the basis of its first oil sales contract, signed by KrymTexasNafta and the Lviv Refinery, the Company booked sales of crude oil produced from its production test wells in the Aktash Field, Crimea. Payments were made in Ukraine currency and used to assist in meeting local operational expenses. Although minimal by comparison with expectations and costs to date, the net proceeds of US$19,389 are an early indication that the Company can expect to earn and accrue revenues from its Ukraine operation.
- The first sale of oil was an important milestone: Epic's transition from an exploration company to a production company.
- Another milestone was the completion of a formal Licensing Agreement covering the shallow oil fields of Crimea with a contingent commitment for the development of the much larger, deeper fields. The Licensing Agreement is based upon the Production Sharing Agreement signed in 1993. It reaffirms Epic's confidence that both Epic and Ukraine will continue to honour their respective legal commitments.

Future Potential

Exploration studies conducted primarily under contract with Krymgeologia have identified a number of high quality drilling targets for additional shallow oil reserves. All of these candidates are in the Kerch Peninsula portion of Crimea and some have had test wells drilled in them by Krymgeologia, confirming the presence of oil-rich reservoirs.

Other geotechnical studies have delineated six immediate targets for evaluation and future development of large reserves of gas-condensate at depths of 2400 - 4600 metres.

An independent engineering study is proceeding on these field discoveries and exploration drilling targets to provide the Company and the marketplace with qualified proven, probable, and possible reserves of oil and gas. Our initial calculations indicate that at least four of the six deep targets, and seven of the nine shallow oil field targets may be of economically viable field size.

Operational Results

Our original strategy was to run a highly efficient, low-cost operation in Crimea until we proved it would be an economically viable operation. At that point, the Company would be fully capitalized and the funds would be efficiently utilized to rapidly expand production revenues. This strategy was only partially successful. Our successes and failures are discussed under ***Operations Review*** in this annual report.

Most importantly, Epic has successfully determined that it can operate an oil and gas company in Crimea cost-effectively, with sufficient support from Ukraine, to forecast a successful program that will provide an excellent return on its shareholders' investment.

Outlook for the Next Year

We have just recently completed the re-capitalization of Epic's Ukraine projects through an equity financing of $20 million, gross proceeds. The planned use of proceeds are split between the development of the shallow oil fields program and the detailed evaluation of the deeper gas-condensate field discoveries. In future letters to the shareholders, we will discuss the Company's plans and targets for production and income.

Shallow Oil Fields

The results from our test production wells indicate that the most productive and effficient method to develop these fields will be with closely-spaced (30 acre spacing) production wells. Although capable of higher rates of production, the wells will be produced at rates in the range of 100 to 250 barrels per

day. At high production rates, the friable clays accumulate in the well bore. Thus, with a greater well density, total production will be as high as originally planned, and with lower maintenance costs.

We have targeted seven shallow field discoveries for confirmation wells and subsequent development. Our aggressive goal is to drill as many as 100 wells in 1997 with additional drilling and completion rigs operated by Ukrainian crews. Revenues from the increased production are expected to cover the capital and operating costs beyond the forecasted $3.8 million exposure.

Deep Oil-Gas-Condensate Fields

The exciting potential of the deeper field discoveries may well turn out to be Epic's highest priority. Together with Krymgeologia (KG) personnel in Simferopol, Crimea, we will re-process a substantial volume of KG's seismic data. Comprehensive feasibility studies will be completed on at least six field discoveries that have calculated possible reserves of more than one trillion cubic feet of gas and 50 million barrels of condensate. The number of wells already drilled in these field discoveries ranges from one, in one very large structure, to more than 17 in at least two cases.

By mid-year, Epic expects to acquire 3-D seismic data across one of the most promising field discoveries.

During 1997, we plan to drill a new test well in one of these deep fields, which range from 2,400 to 4,600 metres. Where possible, we will re-enter and try to re-complete at least two of the preserved Ukraine wells. The Company believes that by drilling with balanced muds we may find additional oil reservoirs.

These efforts will be conducted concurrently with the development of the shallow oil fields and we expect to be able to announce, before the end of 1997, a decision to develop one of these large gas-condensate fields.

Ronald K. Cormick
President & CEO

Robert O. Anderson
Chairman

November 8, 1996

OPERATIONS REVIEW

Summary

Our Crimean operations proceeded at a slower pace than expected. Nevertheless, we made significant progress in a number of areas critical to our transformation from an expense-based exploration company to a revenue-generating international oil production company.

Successes:

- we have resolved the critical operating issues;
- we have shown that we can overcome the bureaucracy, use local personnel and drill wells in Crimea;
- the Ukraine data has been proven to be basically reliable, and there **are** field discoveries throughout Crimea;
- we can produce oil, transport and store it without it being stolen;
- we can sell crude oil in Ukraine and get paid upon delivery;
- we can keep or reinvest the revenues;
- the Ukraine authorities honour their agreements;
- we have learned how to operate at very low costs, using a combination of Ukrainian and western personnel, equipment, and materials;
- our team of experts who learned international operations substantially under the huge financial umbrellas of the *majors* can work well without it;
- Epic is capable of developing the small oil fields in Crimea economically for significant benefit to all parties;
- we have a unique opportunity to proceed cost-effectively at a dynamic pace; to start developing the large fields in 1997.

Failures:

- we have missed a number of target dates;
- we have not yet established uninterrupted production;
- we have taken too long to complete the test program;
- we have consumed the hard-earned savings obtained from being a low-cost operation while having to await completion of needed financing.

The achievements of the past year show that Epic has the ability to deal successfully with the uncertainties of operating in Eastern Europe and to do it on an efficient, low-cost basis.

Major Contract Signed

In March, 1996, the Company signed a comprehensive Licensing Agreement with Ukraine covering the exploration and development of all shallow oil fields in the Kerch Peninsula area. The Agreement also provides specific licensing coverage for Epic's planned subsequent development of the deeper and larger oil and gas fields in the same region. The Agreement defines and clarifies the items and issues that are described in general terms in the original Production Sharing Agreement that assigns the Company the right to explore and develop the oil and gas potential of the Crimean Peninsula, in cooperation with its Ukraine partner, Krymgeologia. The Agreement represents a major step in perfecting Epic's legal position in the evolving Ukraine business environment.

The Aktash Field

We focused most of our operational efforts during the year on the Aktash Field, which is a geologically well-defined, small field where core samples and well-log data from shallow delineation wells, drilled in the early 1980's, indicated 6 million barrels of proved and probable oil reserves (Company calculations).

Two additional wells, 103-3 and 115-4, were drilled, tested, and placed in production in the Aktash Field. By the end of the fiscal year, we had drilled, tested, and completed four Aktash wells, which are capable of producing oil at a combined sustained rate of 400 to 600 barrels per day. This is less than actually tested but judged to be the best rates for lowest production maintenance and for maximum ultimate recovery of oil.

While drilling just four wells is not an impressive total in itself, the Company designed this test program to minimize financial exposure and risk while ascertaining the overall viability of overcoming difficult logistical, political, bureaucratic, and technical problems that often confront energy companies operating in developing nations like Ukraine.

We believe we have now solved the significant drilling and completion problems in this field. The last well drilled in our four-well test program, well 115-4, is a flowing well, without any attendant clay maintenance problems.

The local operating company, KrymTexasNafta, has knowledgeable staff who have been increasingly successful at procuring goods and services from local sources. This accomplishes two important objectives: it contributes directly to the Ukraine economy; and, it is also cost-effective on the basis of price and delivery times.

It is important to note that all of our operations have been accomplished with Ukrainian drilling and production personnel who were initially trained and supervised by our Western managers. This success is in large part due to the willingness of our personnel to meld culturally in order to deal effectively, both

professionally and personally, with the local labor force. Credit must also be given to the Ukrainian employees, who have been eager to learn how to operate Western style drilling equipment and to perform well in a new work culture. We believe that this melding of equipment, technology, and cultures is by far the most important operational achievement of our partnership venture. It bodes well for our future success, as the expenditures increase and the program expands.

First Oil Sales

In February 1996, KrymTexasNafta signed a contract for the initial sale of crude oil from the Aktash Field. The oil is being sold to the Lviv Pilot Refinery Plant in Lviv, Ukraine, at a higher price, and transported at a lower cost than we expected when we did our earlier financial projections. The net-after-transportation price is approximately US$18 per barrel. The sweet, naphthenic-rich oil produced at Aktash has an API gravity of between 23 and 25 degrees. Since the Lviv Refinery specializes in the production of lubricating oils, it is willing to pay world market prices for the high quality crude available from Aktash.

Next Steps in Exploration and Development

The initial test program completed in the Aktash Field fully confirmed the viability of operating in this region and laid a solid foundation for the scheduled rapid development of the Aktash Field. In addition, it confirms that Epic can economically develop the smaller oil fields in Crimea and can now move at a faster pace to begin developing the much larger fields.

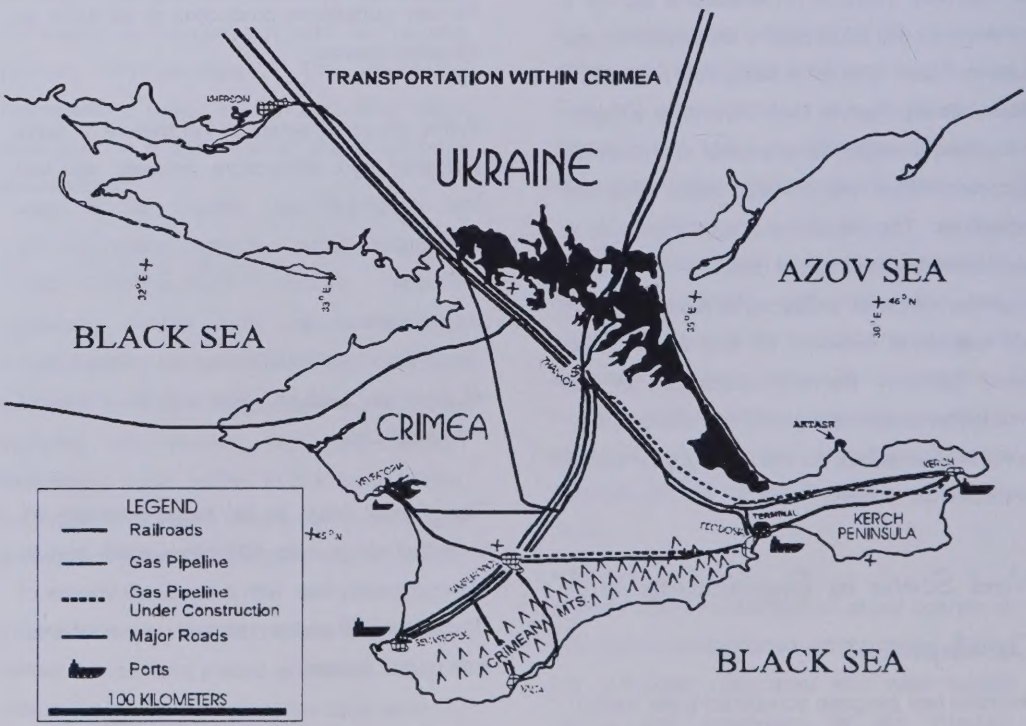
Concurrent with the development of the Aktash Field, Epic also plans to test and develop several nearby shallow oil fields that have combined proven, probable, and potential reserves of more than 28 million risked-barrels of recoverable oil. Current forecasts indicate that, over a three-year period, more than 250 shallow wells will be drilled and brought into production, providing an estimated maximum daily production of 21,000 barrels of oil, and a 15-year cumulative production of as much as 43 million barrels.

While the development of the shallow oil fields proceeds, Epic will explore, evaluate, and test the higher-potential, deeper oil & gas-condensate fields. Current plans call for extensive seismic re-processing and interpretation, a 3-D seismic survey, comprehensive feasibility studies, working over of preserved Ukraine wells, and the drilling of new test wells.

The deeper fields to be evaluated have an indicated range from 100 billion cubic feet to 1.5 trillion cubic feet, with a combined volume of more than 50 million barrels of associated natural gas liquids.

As Epic's production increases, the oil will be sold primarily on the world market for US dollars. It will be transported on small (15,000 to 60,000-ton) shallow-draft, double-hulled

tankers that will load at the oil port of Feodosia, Crimea (see map below), where the Company plans to invest an estimated $1.5 million to upgrade oil terminal and offshore loading facilities. This will improve the Company's transportation efficiency and greatly reduce environmental risk. These tankers encounter no restrictions of passage through the Bosphorous and Dardanelles into the Mediterranean Sea. Because of the high quality of the oil, and subsequent condensate, Epic will probably be able to sell its oil at a premium over standard Black Sea oil prices for oil with 23-25° API.



MANAGEMENT'S DISCUSSION AND ANALYSIS

Management is responsible for the preparation of the consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for ensuring that all other financial and operating information presented in this annual report are consistent with such consolidated financial statements. Management has established and maintains a system of internal controls which are designed to provide assurance that assets are managed efficiently and to facilitate the preparation of reliable and timely financial information.

Independent auditors appointed by the shareholders of the Company have examined the consolidated financial statements. The Audit Committee has reviewed these financial statements with management and the auditors and has reported to the Board of Directors. The Board of Directors has approved the consolidated financial statements.

The Management's Discussion and Analysis is presented to provide the reader with a detailed analysis of the overall performance of the Company for the most recently completed fiscal year. The information provided in the report reflects data available as of November 15, 1996. Some assumptions are based on estimated results and may in fact vary from actual results.

Financial Highlights

Improved financial performance during 1995 resulted directly from the successful drilling of oil producing test wells in Crimea and successful financing via private placements during the year.

As of the end of the fiscal year, June 30, 1996, oil sales to the Lviv Refinery had begun and the Company had received a net of US$19,389. Average price per barrel of oil, net of transportation costs was $18.50.

Epic's net revenues per barrel (*net back)* cannot be determined at this time. Several of the local tax collectors have not yet received official notification from the government regarding the local operating company's exemptions. For example, KrymTexasNafta (KTN) is exempt from income tax for at least 5 years, from VAT during cost-recovery, and from a new rental fee imposed on other oil and minerals projects. KTN is grandfathered by the *Enterprises with Foreign Investment* Laws.

As at June 30, 1996, the Company has not yet achieved *commercial production*. As a result, the financial statement may appear unusual when compared with those of other operating oil companies.

The expenditures charged during this fiscal year to the Company's oil and gas interests in Crimea, Ukraine, were $849,490. After other adjustments, the total oil and gas interests increased from $6,051,627 to $6,675,650.

During this same period, expenses charged against Corporate operations increased from $1,567,843 charged in 1995 to $1,983,441 charged in 1996. This increase was primarily due to the increased efforts by Epic to obtain equity financing for the Company's Ukraine project.

To finance these project and corporate expenditures, Epic privately placed a total of 3,521,923 special warrants for a gross proceeds of US$2,180,338. Assuming all share purchase warrants are exercised, the fully diluted impact of these private placements is an additional 3,094,295 common shares. Together with all outstanding warrants and options, this represents a total of 48,449,099 common shares on a fully diluted basis.

Net losses for 1996 were $2,196,424 compared to $1,567,843 for 1995. That amounted to a net loss per share of $0.058 for 1996 compared to $0.054 for 1995. The total deficit was increased from $3,440,856 to $5,637,280.

Operations

The second half of the fiscal year saw a strengthening of oil prices worldwide. Black Sea spot market prices continue to be very competitive with North Sea prices.

However, the production levels have not yet reached the capacity of the Lviv Refinery. As long as the refinery continues to pay world market prices, net after transportation, it will be in Epic's best interests to continue selling its production share to them.

Recent information has determined that the refinery is capable of processing almost 7,000 barrels per day. This would allow the Company more time to complete the negotiations and to upgrade the Feodosia oil terminal and tanker loading facilities. The Company's aggressive drilling program forecasts gross production to exceed 7,000 barrels per day late in 1997.

On behalf of Management

Ronald K. Cormick
CEO and President

ATTACHMENTS

1996 Annual Report

KPMG
Chartered Accountants

Box 10426 777 Dunsmuir Street
Vancouver BC V7Y 1K3 Canada

Telephone (604) 691-3000
Telefax (604) 691-3031
http://www.kpmg.ca

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Epic Energy Inc. as at June 30, 1996 and 1995 and the consolidated statements of operations and deficit and changes in financial position for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at June 30, 1996 and 1995 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

KPMG

Chartered Accountants

Vancouver, Canada

October 15, 1996, except as to note 14 which is as of November 8, 1996

CONSOLIDATED FINANCIAL STATEMENTS

EPIC ENERGY INC.

Consolidated Balance Sheets
(In U.S. Dollars)

June 30, 1996 and 1995

	1996	1995
Assets		
Current assets:		
Cash	$ 25,281	$ 587,554
Accounts receivable	45,274	55,258
Note receivable (note 4)	50,000	50,000
	120,555	692,812
Oil and gas interests (note 5)	6,675,650	6,051,627
Mineral properties and deferred exploration (note 6)	–	284,095
	$ 6,796,205	$ 7,028,534
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities (note 12(b))	$ 624,001	$ 974,761
Notes payable (note 7)	–	535,704
Loan payable (note 11(c))	–	72,860
Accrued interest payable	–	29,058
Payable to HyTEXplor Houston Inc.	132,890	420,166
	756,891	2,032,549
Preferred shares issued by subsidiary (note 8)	280,000	280,000
Shareholders' equity:		
Share capital (note 9)	4,395,603	3,259,299
Special warrants (note 9(c))	2,103,449	–
Contributed surplus	4,897,542	4,897,542
Deficit	(5,637,280)	(3,440,856)
	5,759,314	4,715,985
Nature of operations (note 1)		
Commitments and contingencies (note 11)		
Subsequent event (note 14)		
	$ 6,796,205	$ 7,028,534

See accompanying notes to consolidated financial statements.

On behalf of the Board:

______________ Director ______________ Director

EPIC ENERGY INC.

Consolidated Statements of Operations and Deficit
(In U.S. Dollars)

Years ended June 30, 1996 and 1995

	1996	1995
Expenses:		
Administration fees to HyTEXplor Houston Inc.	$ –	$ 348,002
Contract services	268,526	235,021
Directors' fees for attendance at meetings	–	13,000
Interest on notes payable	12,869	33,667
Investor relations	120,909	39,354
Mobilization costs	–	124,605
Office and miscellaneous	446,010	157,606
Professional fees	358,296	134,858
Salaries and benefits	461,175	361,662
Travel	315,656	120,068
Loss from operations	1,983,441	1,567,843
Other expenses (income):		
Write-off of mineral properties and deferred exploration (note 6)	284,095	–
Write-off of Oklahoma, U.S.A., oil and gas interests	6,078	–
Gain on settlement of debt (note 10)	(77,190)	–
	212,983	–
Loss for the year	2,196,424	1,567,843
Deficit, beginning of year	3,440,856	1,873,013
Deficit, end of year	$ 5,637,280	$ 3,440,856
Loss per share	$ 0.058	$ 0.054

See accompanying notes to consolidated financial statements.

EPIC ENERGY INC.

Consolidated Statements of Changes in Financial Position
(In U.S. Dollars)

Years ended June 30, 1996 and 1995

	1996	1995
Cash provided by (used in):		
Operations:		
Loss for the year	$ (2,196,424)	$ (1,567,843)
Write-off of mineral properties and oil and gas interests, an item not involving cash	290,173	–
Changes in non-cash working capital:		
Accounts receivable	9,984	(32,593)
Accounts payable and accrued liabilities	(350,760)	382,020
	(2,247,027)	(1,218,416)
Financing:		
Increase (decrease) in payable to HyTEXplor Houston Inc.	(287,276)	(4,024,946)
Increase in contributed surplus	–	4,897,542
Notes and accrued interest payable	(564,762)	551,964
Loan payable	(72,860)	72,860
Issue of convertible preferred shares	–	1,440,408
Issue of common shares and special warrants	412,366	1,817,841
Special warrant subscriptions received (note 9)	2,103,449	–
Issue of common shares on settlement of debt	723,938	–
	2,314,855	4,755,669
Investments:		
Proceeds from sale of rights (note 4)	–	50,000
Oil and gas interests, net	(630,101)	(1,098,305)
Business combination, net of $12,431 cash (note 3)	–	(1,860,099)
Note receivable	–	(50,000)
	(630,101)	(2,958,404)
Increase (decrease) in cash	(562,273)	578,849
Cash, beginning of year	587,554	8,705
Cash, end of year	$ 25,281	$ 587,554

See accompanying notes to consolidated financial statements.

EPIC ENERGY INC.

Notes to Consolidated Financial Statements
(In U.S. Dollars)

Years ended June 30, 1996 and 1995

The Company was incorporated under the Company Act (British Columbia) on July 8, 1992 as OTM International Development Inc. The Company changed its name to Epic Energy Inc. on April 6, 1995 and continued under the Business Corporations Act (Alberta) on April 15, 1996. Its principal business activity involves the exploration and development of its oil and gas properties. The Company has the rights under a production sharing agreement with Krymgeologia ("KG"), a State Geological Enterprise established in the Republic of Crimea, Ukraine (the "Production Sharing Agreement") to develop the petroleum potential of an area approximating 11,000 square miles in the Republic of Crimea. Prior to November 10, 1994, the Company's legal subsidiary also had rights under the Production Sharing Agreement to develop the petroleum potential of an area approximating 4,000 square miles in South West Ukraine (note 4).

1. Nature of operations:

The Company is in the process of exploring its oil and gas properties. The recoverability of the Company's investment in its oil and gas interests is dependent upon the existence and discovery of economically recoverable oil and gas reserves, confirmation of the Company's interest in the oil and gas interests, the ability of the Company to obtain necessary financing to complete development of the interests, and upon the ability to attain future profitable production.

The Company is in the process of obtaining independent reserve reports on its oil and gas interests.

2. Significant accounting policies:

(a) Basis of consolidation:

These consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries HHO Ltd. and Epic Energy Inc., (incorporated in Delaware, USA) and its 98.2% owned subsidiary HHO (Aktash) Limited. HHO Ltd. and HHO (Aktash) Limited are incorporated in the States of Jersey, Channel Islands.

(b) Functional currency

As a majority of the Company's operations are conducted in U.S. dollars, a majority of its shareholders are not residents of Canada, and any future revenues will be denominated in U.S. dollars, the U.S. dollar has been chosen as the Company's functional currency.

2. Significant accounting policies (continued):

(c) Oil and gas interests:

The Company follows the full cost method of accounting for oil and gas interests whereby all costs of exploring and developing oil and gas reserves are capitalized. Such costs include land acquisition costs, geological and geophysical expenses, and overhead charges directly related to acquisition, exploration and development activities.

The Company's petroleum and gas interests are unproven properties and as such are not subject to depletion. These costs will be reviewed periodically to ascertain whether impairment has occurred. If impairment occurs, the costs will be written down to their estimated net realizable value.

If and when proven reserves are assigned to the petroleum and gas interests, the costs will be depleted on the unit-of-production method based on the estimated gross proven reserves as determined by the Company. In addition, the costs less accumulated depletion will be limited to an amount equal to the estimated future net revenue from proven reserves (based on unescalated prices and costs at the balance sheet date) less estimated future general and administrative expenses, financing costs and income taxes.

(d) Mineral properties and deferred exploration:

During the year ended June 30, 1996 the Company's option to acquire an interest in certain mineral properties expired. The Company has written off its mineral properties and deferred exploration (note 6).

(e) Foreign currency translation:

Transactions of the Company that are denominated in foreign currencies are recorded in U.S. dollars at exchange rates in effect at the related transaction dates. Monetary assets and liabilities denominated in foreign currencies are adjusted to reflect exchange rates at the balance sheet date. Exchange gains and losses arising on the translation of monetary assets and liabilities are included in the determination of income for the year.

(f) Loss per share:

Loss per share has been calculated using the weighted average number of common shares outstanding during the period.

(g) Comparative figures:

Certain comparative figures have been restated to conform with presentation adopted in the year ended June 30, 1996.

(In U.S. Dollars)

3. Business combination:

By a share exchange agreement dated November 10, 1994, and effective on the closing date of February 15, 1995, the Company acquired 100% of the issued and outstanding shares of HHO Ltd., being 220,000 ordinary shares, in consideration for the issuance of 5,000,000 common shares and 20,000,000 Series A preferred shares in the share capital of the Company. The Series A preferred shares are convertible into common shares by the holder thereof on the basis of one common share for each Series A preferred share. The 20,000,000 Series A preferred shares were converted to common shares prior to June 30, 1995 (note 9(b)). Pursuant to the terms of the share exchange agreement, the Company has issued an additional 1,000,000 common shares as a finder's fee.

Since this transaction resulted in the former shareholders of HHO Ltd. owning the majority of the issued shares of the Company, the exchange has been treated for accounting purposes as an acquisition by HHO Ltd. of the net assets and liabilities of the Company. On this basis of accounting:

(a) HHO Ltd. is deemed to be the purchaser for accounting purposes. Accordingly, the consolidated financial statements after the combination reflect the assets, liabilities and deficit of HHO Ltd. at their previous book values, as well as the net assets of the Company at their fair values. The number of issued shares reflect the issued shares of the Company, which is recorded at the amount of issued capital of HHO Ltd. increased by the fair value of the net assets of the Company.

The consolidated financial statements for the period ended June 30, 1995 reflect the results of operations of HHO Ltd., which include the Company's operations from the effective date of the business combination.

(b) The Company, the legal parent, is deemed for accounting purposes to be a continuation of HHO Ltd., the legal subsidiary. Control of the net assets and liabilities of the Company was acquired effective February 15, 1995, for total consideration equal to the fair value of the Company's net assets on that date as follows:

Cash	$ 12,431
Accounts receivable	22,665
Investment in oil and gas joint venture with HHO Ltd.	1,672,800
Other oil and gas interests	6,078
Mineral property and deferred exploration	284,095
	1,998,069
Accounts payable and accrued liabilities	(125,539)
Net assets acquired	$ 1,872,530
Consideration given has been allocated as follows:	
5,000,000 common shares	$ 360,102
Finders fee of 1,000,000 common shares	72,020
20,000,000 Series A preferred shares	1,440,408
	$ 1,872,530

(In U.S. Dollars)

3. Business combination (continued):

The assets and liabilities of the Company acquired effective February 15, 1995 have been translated to U.S. dollars at the exchange rate in effect at that date.

4. Note receivable:

By shareholder resolution effective November 10, 1994, HHO Ltd. resolved to transfer its rights under the Production Sharing Agreement for property in South West Ukraine (approximately 4,000 square miles) to a separate legal entity owned by the original shareholders of HHO Ltd., for consideration of a promissory note with a face value of $50,000. The note was due on January 1, 1996 and until this date bore interest at 6% per annum. The note is in default and under the terms of the promissory note now bears interest at 8% per annum.

5. Oil and gas interests:

	1996	1995
Republic of Crimea, Ukraine:		
Deferred exploration costs:		
Geological and geophysical expenses charged by HyTEXplor Houston Inc.	$ 3,416,784	$ 3,416,784
Costs capitalized on acquisition of Production Sharing Agreement from HyTEXplor Houston Inc.	703,442	703,442
Drilling equipment	1,233,135	823,015
Transportation	620,723	579,391
Travel	85,771	76,306
Professional fees	152,271	47,788
Exploration services	31,606	21,885
Personnel	445,810	230,348
Office equipment	70,520	60,095
Insurance	19,642	15,842
Other	165,335	120,653
	6,945,039	6,095,549
Less proceeds from sale of rights to the south west Ukraine area under the Production Sharing Agreement (note 4)	(50,000)	(50,000)
Less non-refundable deposit received for a non-executed letter of intent	(200,000)	–
Less net proceeds from start-up production	(19,389)	–
	6,675,650	6,045,549
Oklahoma, U.S.A.:		
Acquisition	–	1,109
Participation	–	4,969
	–	6,078
Total oil and gas interests	$ 6,675,650	$ 6,051,627

5. Oil and gas interests (continued):

(a) Republic of Crimea, Ukraine:

The Company acquired its rights under the Production Sharing Agreement with KG, the State Geological Enterprise established in the Republic of Crimea, from HyTEXplor Houston Inc. ("HHI"), the parent of HHO Ltd. at that time. Consideration given for the Production Sharing Agreement included the assumption of liabilities in an amount equivalent to the costs charged by HHI on the project to date, the commitment to issue 5,000 convertible preferred shares, and the over-riding royalty interest described in note 11(a). Liabilities assumed in respect of costs charged by HHI up to the acquisition date total $998,818 of which $703,442 was capitalized within oil and gas interests. All subsequent costs of exploring and developing oil and gas properties under the Production Sharing Agreement have been capitalized. The 5,000 convertible preferred shares were issued by HHO Ltd. in the year ended June 30, 1994. The Production Sharing Agreement includes the rights to conduct Petroleum Operations in the Area (as defined) and to lift, dispose of, sell and export the Company's share of such petroleum and to repatriate or retain abroad the proceeds from the sale.

The Company has the right to determine the feasibility of developing the fields within the Area, and to participate in the exploration, development and production of oil, gas and condensate in the Area.

The Company is to bear all costs and expenses required in carrying out all the Petroleum Operations. The Production Sharing Agreement allows up to 50% of the total production revenues to be received by the Company as cost recovery with the remaining production being allocated 60% to the Company and 40% to KG. The Production Sharing Agreement is for a period of 25 years with a 15 year extension at the option of the Company.

A jointly owned limited liability Crimean company, Krymtexasnafta Ltd. ("KTN") has been formed by the Company and KG to conduct the petroleum operations under the Production Sharing Agreement.

During the year ended June 30, 1996, KTN was granted a license by the Ukrainian State Committee on Geology and the Utilization of Mineral Resources for the exclusive exploration, development and production of and for petroleum in a portion of the area covered by the Production Sharing Agreement approximating 5,400 square kilometres in eastern Crimea.

(b) Oklahoma, U.S.A.:

By agreement dated July 22, 1992, the Company acquired an interest in a 1,700 acre petroleum and natural gas prospect in Grant and Garfield Counties, Oklahoma, U.S.A. The first prospect drilled is known as the Sally Annette #1-28 well in which the Company has a 1% working interest. The Company has written off this prospect in the year ended June 30, 1996.

(In U.S. Dollars)

6. Mineral properties and deferred exploration:

	1996	1995
Mineral properties	$ –	$ 28,705
Deferred exploration	–	255,390
	$ –	$ 284,095

(a) R and W Mineral Claim:

By agreement dated March 11, 1993, the Company acquired all rights, title, and interest to the R and W Mineral Claim, located in the Revelstoke Mining Division, British Columbia, from a director of the Company for total consideration of Cdn. $40,000. During the year ended June 30, 1996 the Company has written off the mineral property.

(b) Brew 1-7 Mineral Claims option agreement:

By agreement dated March 25, 1993, the Company was granted an option to acquire a fifty percent interest in the Brew 1-7 Mineral Claims, located in the Revelstoke Mining Division, British Columbia. To exercise the option, the Company was required to incur expenditures on or related to exploration on the Brew 1-7 and the R and W Claims aggregating Cdn. $500,000 by March 24, 1996. This condition was not met and the Company has written off the deferred exploration costs for the year ended June 30, 1996.

7. Notes payable:

At June 30, 1995, notes payable of $296,800 were due to directors or former directors and bore interest at 10% per annum. The remaining $238,904 of the notes payable were due to third parties. At June 30, 1995 all of the notes payable were in default. During the year ended June 30, 1996 the Company settled the notes payable with cash payments and issuances of common shares of the Company (note 9).

8. Preferred shares issued by subsidiary:

HHO (Aktash) Limited has issued 280 preferred shares to third parties for proceeds of $280,000. Holders of each of the preferred shares are entitled to a cumulative dividend at the annual rate of 0.00375% of annual revenues before general and administrative costs from the production from the Aktash field and the first two economically viable satellites of the Aktash field that are developed by the Company. The preferred shares are to be redeemed on June 30, 2003 at their stated value of $280,000.

(In U.S. Dollars)

9. Share capital:

(a) Authorized:

Unlimited (1995 - 200,000,000) common shares without par value

Unlimited (1995 - 50,000,000) preferred shares without par value with the directors to issue the preferred shares in series, to fix the number of shares and designation of each series of preferred shares, and to create and attach special rights and restrictions to each series.

(b) Issued:

	Number of shares	Amount
Common shares:		
Balance, June 30, 1994	1,578,579	$ 1,050
Issued during the period ended February 15, 1995	2,000,000	162,555
On acquisition of the net assets of the Company at fair market value (note 3(b))	5,000,000	360,102
Finders fee on acquisition (note 3(b))	1,000,000	72,020
Conversion of preferred shares issued on acquisition (note 3(b))	20,000,000	1,440,408
Exercise of Special A warrants	4,400,000	1,578,758
Bonus shares issued on Special A warrants	440,000	–
Exercise of Special B warrants	1,125,007	605,490
Exercise of warrants	1,767,800	966,011
Adjustment required by accounting principles of business combinations	–	(1,650,751)
Share and special warrant issue costs	–	(276,344)
Balance, June 30, 1995	37,311,386	3,259,299
Issued during the year:		
For cash on exercise of agents' options	200,000	36,510
For cash on exercise of options	250,000	100,093
For cash on private placement	407,500	299,831
Settlement of debt	586,910	723,938
Share issue costs	–	(24,068)
Balance, June 30, 1996	38,755,796	$ 4,395,603

The shares issued by the Company before the reverse take over transaction of February 15, 1995 described in note 3 are recorded above at a value of nil and the dollar amounts shown above are the amounts as recorded by HHO Ltd. as at and during each of the periods noted above to February 15, 1995. The number of shares shown as outstanding represents the legal capital of the Company.

(In U.S. Dollars)

9. Share capital (continued):

(b) Issued (continued):

	1996	1995
Preferred shares:		
20,000,000 Series A preferred shares issued on acquisition of the net assets of the Company at fair market value(note 3(b))	$ –	$ 1,440,408
Conversion to 20,000,000 common shares	–	(1,440,408)
	$ –	$ –

Holders of the Series A preferred shares could, at their option, at any time after the latest date of a receipt issued with respect to a prospectus filed in the Provinces of Alberta and British Columbia, convert all or part of the Series A preferred shares held by such holder into common shares of the Company on the basis of one common share for each Series A preferred share held on the date of conversion. All Series A preferred shares were converted to common shares prior to June 30, 1995.

(c) Special Warrants:

	1996	1995
2,666,666 Special Warrants at Cdn.$0.75 per Special Warrant. Each Special Warrant entitles the holder to acquire one common share and one share purchase warrant up to December 7, 1996 without further payment. Each share purchase warrant entitles the holder to acquire one common share at an exercise price of Cdn.$1.00 prior to December 7, 1996	$ 1,460,387	$ –
204,348 Special Warrants at Cdn.$1.30 per Special Warrant Each Special Warrant entitles the holder to acquire one common share and one-half share purchase warrant up to August 31, 1997 without further payment. Each share purchase warrant entitles the holder to acquire one common share at an exercise price of Cdn.$1.65 prior to August 31, 1997	193,132	–
650,909 Special Warrants at Cdn.$1.10 per Special Warrant. Each Special Warrant entitles the holder to acquire common share and one-half purchase warrant up to October 26, 1997 without further payment. Each share purchase warrant entitles the holder to acquire one common share at an exercise price of Cdn.$1.50 prior to October 26, 1997	526,819	–
Less issue costs	(76,889)	–
	$ 2,103,449	$ –

(In U.S. Dollars)

9. Share capital (continued):

(c) Special Warrants (continued):

Each of the 4,400,000 Special A Warrants issued in the 1995 fiscal year at Cdn.$0.50 each entitled the holder thereof to acquire, at no additional cost to the holder, upon exercise, one unit consisting of one common share of the Company and one-half of a share purchase warrant ("Warrant"). Any Special A Warrants not exercised on the expiry date were deemed to be exercised. Each Warrant entitled the holder to acquire one additional common share of the Company at any time up to June 30, 1995 upon the payment of the exercise price of Cdn. $0.75 per common share.

Each of the 1,125,007 Special B Warrants issued in the 1995 fiscal year at Cdn.$0.75 each entitled the holder thereof to receive, at no additional cost, up to June 30, 1995, one common share of the Company. Any Special B Warrants not exercised on the expiry date were deemed to be exercised.

(d) Options and warrants:

The Company has 2,873,335 (1995 - 1,305,000) options outstanding to acquire common shares of the Company. 2,673,335 (1995 - 1,105,000) of these options have been issued to directors, officers, employees and consultants of the Company and 200,000 (1996 - 200,000) to agents of the Company.

Details of options outstanding are as follows:

Expiry date	Exercise price	Number of options 1996	1995
February 28, 1998	Cdn. $0.50	655,000	855,000
February 28, 1998	1.00	200,000	250,000
November 28, 1998	1.00	1,450,000	–
January 29, 1999	1.25	73,335	–
June 30, 1999	1.00	195,000	–
June 6, 1997	1.00	100,000	–
September 12, 1997	0.75	200,000	–
January 10, 1996	0.25	–	200.000

In addition, the Company has 203,750 (1995 - nil) share purchase warrants outstanding entitling the holder to purchase one common share of the Company at a price of $1.50 exerciseable until October 26, 1997 and has share purchase warrants outstanding in respect of special warrants financings as disclosed in note 9(c).

10. Gain on settlement of debt:

During the year ended June 30, 1996, the Company settled debt with its creditors at a discount. This gain represents forgiveness of debt less related costs of settlement.

11. Commitments and contingencies:

(a) Overriding royalty interest:

As part of the consideration for the acquisition of the Production Sharing Agreement (note 5(a)), the Company has committed an overriding royalty interest to HHI on production revenues from the first three fields to be developed in the area covered by the Production Sharing Agreement. The royalty is defined as 10% of production revenues from the first field to be developed (Aktash and its satellites) and 6.25%, and 4.5%, respectively, of production revenues from the second and third fields to be developed.

(b) Profit share:

The Company has sold to investors a total committed profit share of 1.05% of net revenues, before general and administrative costs, from the production of the Aktash field and the first two economically viable satellite fields that are developed thereafter as described in note 8. In addition, the rights under the Production Sharing Agreement relating to the Aktash field and the first two satellite fields are to be transferred to HHO (Aktash) Limited.

(c) Loan payable:

As consideration for providing a loan in a prior year, the Company granted to the lender a right to earn up to a 50% working interest, but not less than a 20% working interest, on the first precious metals project in the Ukraine that the Company may obtain rights to in the future.

(d) Directors' compensation:

The Company is committed by a Board resolution, that two (1995 - three) former directors of the Company as of December 16, 1993 each receive a vested interest representative of 3/10ths of one percent of the total production revenues of the fields included in the present Production Sharing Agreement, such participation to be for a period of 15 years from the commencement date of production from the initial field. In no event shall the total remuneration under this bonus plan exceed U.S. $3,000,000 for each of the two directors. Total production revenue, for purposes of this calculation, shall mean the total sales revenue from the sale of hydrocarbons less the direct costs associated with getting such hydrocarbons to market (i.e., sales less direct cost of goods sold).

(e) KTN fund for the Development of Crimea:

Under the terms of the license agreement described in note 5(a), KTN is required to pay 0.25% of its income before taxation to a special fund called the KTN Fund for the Development of Crimea. The fund will be owned by KTN and is to be utilized for the improvement of Crimea.

(In U.S. Dollars)

11. Commitments and contingencies (continued):

(f) Lease commitments:

The Company and its subsidiaries lease office space under operating leases expiring at various dates to 2001. The minimum lease payments are as follows:

1997	$ 87,004
1998	89,616
1999	84,651
2000	46,332
2001	38,780
	$ 346,383

12. Related party transactions:

(a) Prior to June 30, 1995 the Company had contracted HHI to assist and consult in the management of the oil and gas exploration, development and production activities in the Ukraine under the Production Sharing Agreement. Time charges were billed by HHI at agreed hourly rates ranging from $30 to $165 per hour, depending on the related experience of the individuals working on the project. Costs incurred on behalf of the Company were billed at cost and the costs of outside consultants have been billed at cost plus a 15% management fee.

Total charges billed by HHI to the Company were nil (1995 - $1,024,001).

The amount payable to HHI at June 30, 1996 was $132,890 (1995 - $420,166).

HHO Ltd. acquired its rights under the Production Sharing Agreement from HHI. HHO Ltd. and HHI are related by common management and shareholders prior to the business acquisition described in note 3. HHI is controlled by the controlling beneficial shareholders of the Company.

(b) Included in contract services is $107,689 (1995 - $200,018) in consulting fees charged by directors and former directors of the Company and HHO Ltd.

Included in professional fees is $152,067 (1995 - $111,209) in legal fees charged by a law firm of which a director of the Company is a partner.

Included in accounts payable and accrued liabilities are amounts payable to directors and officers of the Company and HHO Ltd. and former directors of HHO Ltd. or to entities related to the directors and former directors of HHO Ltd. of $308,224 (1995 - $582,300).

(In U.S. Dollars)

13. Segmented information:

The Company operates in two industry segments, being the oil and gas and mineral property exploration industries. All of the Company's loss for the years ended June 30, 1996 and 1995 was derived from the oil and gas industry, except for $284,075 of mineral property related costs written off in the year ended June 30, 1996. The carrying amount of identifiable assets in the mineral property exploration industry was nil (1995 - $284,095) with all other identifiable assets in the oil and gas industry.

The Company's operations and assets are located in three geographic segments, being the Republic of Crimea, Ukraine; Canada; and U.S.A. All of the Company's loss for the years ended June 30, 1996 and 1995 was derived from the operations related to the Republic of Crimea, Ukraine except for $284,095 of Canadian mineral properties and $6,078 of Oklahoma, U.S.A. oil and gas interests written off in the year ended June 30, 1996. The carrying amount of identifiable assets related to each of the geographic segments are as follows:

	1996	1995
Republic of Crimea, Ukraine	$ 6,692,607	$ 6,738,361
Canada	41,110	284,095
U.S.A.	62,488	6,078
	$ 6,796,205	$ 7,028,534

14. Subsequent event:

Subsequent to the year end, the Company has completed a private placement of 20,000,000 special warrants at $1.00 per special warrant for gross proceeds of Cdn.$20,000,000. Upon exercise, the special warrant holders will receive, for no additional consideration, one common share of the Company and one-half of one common share purchase warrant, with each whole share purchase warrant entitling the holder to purchase an additional common share for Cdn.$1.20 per share for a period of one year. One-half of the gross proceeds have been placed in escrowed pending receipt for a prospectus qualifying the securities issuable on exercise of the special warrants. In the event that the receipts are not obtained within 120 days of the date of closing, investors will be entitled to either a prorata refund of the escrowed funds or 110% of the securities issuable on exercise of the special warrants.

CORPORATE INFORMATION

Head Office
Canada Place, Suite 450
407 - 2nd Street SW
Calgary, AB, T2P 2Y3
Phone: 403.543.5670
Fax: 403.543.5675
epiccan@earthlink.net

Operations Office
14550 Torrey Chase Blvd.,
Suite 450
Houston, TX USA 77014
Phone: 281.537.2552
Fax: 281.537.8484
epicusa@earthlink.net

Legal Counsel
Ogilvie and Company
Calgary, Alberta

B. C. Toms & Co.
London, England

Auditors
KPMG
Vancouver, BC

Transfer Agents
The R-M Trust Company
Vancouver, BC Calgary, AB

Stock Exchange
The Alberta Stock Exchange
Calgary, Alberta

Trading Symbol: EPI

Senior Officers:
Robert O. Anderson
Chairman

Ronald K. Cormick
President & CEO

Bobby P. Long
VP, Intern. Operations

Donald R. Joiner
GM, Ukraine Operations

Larry R. Helmer
Controller, Finance

R. Michael Zwack
Corporate Secretary

Board of Directors:
Robert O. Anderson
Chairman, Epic Energy
New Mexico, USA

Ronald K. Cormick
President, CEO
Houston, Texas, USA

Laurence G. Decore, Q.C.
Counsel, Biamonte, Cairo
Edmonton, Alberta

Bobby P. Long
VP, Intern Operations
Houston, Texas, USA

Rod W. Husband
Consulting Geologist
Vancouver, BC

John B. Zaozirny, Q.C.
Counsel, McCarthy Tetrault
Calgary, Alberta

R. Michael Zwack
Partner, Ogilvie and Co.
Calgary, Alberta

ABBREVIATIONS

BBLS	Barrels
BPD	Barrels per day
BCF	Billions of cubic feet
BOE	Barrels of oil equivalent (10 MCF = 1 Barrel)
MBBLS	Thousands of barrels
MBPD	Thousands of barrels per day
MCF	Thousands of cubic feet
MCFPD	Thousands of cubic feet per day
MCM	Thousands of cubic metres
MMBBLS	Millions of barrels
MMBOE	Millions of barrels of oil equivalent
MMCF	Millions of cubic feet
MMCFPD	Millions of cubic feet per day
NGLs	Natural gas liquids
TCF	Trillions of cubic feet

METRIC CONVERSIONS

To covert from	To	Divide by
Cubic feet	Cubic metres	35.49
Barrels	Cubic metres	6.29
Feet	Metres	3.28
Miles	Kilometres	0.62
Acres	Hectares	2.50